

MARCH/APRIL 2002

CALIFORNIA FRANCHISE TAX BOARD

Tax News

FTB Pubs.1345, 1345A

Handbook, supplement key to successful e-filing



accepted in the Internal Revenue Service's e-file program and you've passed our suitability check, a marketing kit, including booklets 1345 and 1345A will be sent to you.

New this year - you can now fax your signed application direct to us. Original signature is not required to process your application.

If you are an approved e-file provider, you should have received your FTB Pub. 1345, e-file Handbook and FTB Pub. 1345A, the Handbook Supplement. The booklets were included in the marketing kits that were mailed out the last week of December.

These booklets are important to you because they contain valuable information, such as the rules for participating in our e-file program, instructions, new legislation, new forms, and other helpful information to help you e-file your returns.

If you didn't receive one, and you are an approved e-file provider, please call the e-file Help Desk at (916) 845-0353 to request copies of the handbooks.

You can also access our website at www.ftb.ca.gov/elecserv/index.html to download a copy.

If you are not yet in the e-file program, you can call our help desk and request an application (Form 8633). You can also download the application from our website at www.ftb.ca.gov/forms/01_forms/01_8633.pdf. Once you are

Attention tax practitioners:

Franchise Tax Board field offices and our Tax Practitioner Hotline will be closed on April 1, 2002 in observance of Cesar Chavez Day. Field offices and the hotline will also be closed Sunday, April 14, 2002. Our taxpayer service center *is available* on state holidays during the filing season. Call toll-free at (800) 852-5711. Here is a list of the remaining 2002 official state holidays:

Monday, April 1, 2002

Cesar Chavez Day

Monday, May 27, 2002

Memorial Day

Thursday, July 4, 2002

Independence Day

Monday, September 2, 2002

Labor Day

Monday, October 14, 2002

Columbus Day

Monday, November 11, 2002

Veterans Day

Thursday, November 28, 2002

Thanksgiving Day

Friday, November 29, 2002

Day after Thanksgiving Day

Wednesday, December 25, 2002

Christmas Day

Inside. . .

Law allows FTB to disclose tax data to local governments
Page 2

Enterprise zone incentives expire in Mid-Alameda corridor
Page 3

Ask the Advocate: estimated tax penalty
Page 3

Research, development credit
Page 4

Tax forms corrections
page 5

Tax News

Volume 00-2 March/April 2002

TAX NEWS is a bimonthly publication of the Communications Services Bureau, California Franchise Tax Board. Its primary objective is to provide information to income tax practitioners about state income tax laws, regulations, policies and procedures.

Members of the Board:

Kathleen Connell, Chair
State Controller

John Chiang
Chair, State Board of Equalization

B. Timothy Gage
Director, Department of Finance

Executive Officer:
Gerald H. Goldberg

Editor:
Marvin Meek

To update or correct your address or to subscribe to TAX NEWS (send \$12 for a one-year subscription), write:

TAX NEWS
PO Box 2708
Rancho Cordova, CA 95741-2708
or call: (916) 845-7070

To view TAX NEWS on the Internet or to request an electronic mail subscription, contact FTB on our website:
www.ftb.ca.gov

For information about a client's account, contact:

Tax Practitioner Support Unit
phone: (916)845-7057
fax: (916)845-6377

For recorded answers to questions on California taxes, to order forms, or to check on a refund, call:

(800)338-0505
From outside U.S. (916)845-6600

To send a facsimile about a client's account, transmit to:

Electronic Correspondence
(916)845-6377

Information Center
(800)852-5711
From outside U.S. (916)845-6500

Hearing Impaired
TDD (800)822-6268

FTB on the Internet
www.ftb.ca.gov

Printed on recycled paper

New law allows FTB to disclose some tax data to local governments

Effective January 1, 2002, the newly chaptered Assembly Bill 63 (Chapter 915, Statutes of 2001) enacts Revenue and Taxation Code Section 19551.1, authorizing us to disclose limited tax information to local tax officials.

Information available through this new law may assist local governments with the administration of local city business tax requirements.

Beginning with 2001 tax year data, the information we are authorized to disclose is limited to the taxpayer's name, address, social security number or taxpayer identification number, and principal business activity code (PBA Code).

The 2001 tax forms were changed to provide a space on the front page of the return to record the PBA Code as reflected on the taxpayer's Schedule C return.

Remember head of household questionnaire when e-filing

Assuming you e-file – and we all know e-file saves all around – be sure you include form FTB 1540e, head of household questionnaire with the tax return. This year we've made the questionnaire more comprehensive; in fact it's identical to the head of household audit letter we send to taxpayers when we can't determine their eligibility.

By providing a completed form FTB 1540e with your clients return, it will allow us to determine if your head of household clients qualify for the filing status without them having to later respond to an audit letter.

We will only contact your clients if we still can't make a determination based on the information in the form FTB 1540e.

Tax Practitioner Services

The Tax Practitioner Hotline hours for the remainder of the 2002 filing season are as follows:

- Monday through Friday:
8 a.m. to 5 p.m.

From March 2 through April 13, 2002

- Saturdays:
8 a.m. to 4:30 p.m.

The Tax Practitioner Hotline will not be open on April 1 and April 14, 2002.

Tax Practitioner Hotline

Telephone (916) 845-7057
Fax (916) 845-6377

Personal Income Tax Collection

Fax (916) 845-0494

Business Entities Collection

Fax (916) 845-0145

FTB e-file Help Desk

Telephone (916) 845-0353

Mid-Alameda enterprise zone expires; others get extension

Effective October 14, 2001, a portion of the Mid-Alameda Corridor enterprise zone, City of Lynwood, expired.

All remaining enterprise zones that were scheduled to expire this year have been granted a five-year extension from the California Technology, Trade, and Commerce Agency (TTCA).

Here's how the expiration of enterprise zone tax incentives affect taxpayers operating in the City of Lynwood:

The hiring credit is available after the expiration of the enterprise zone for qualified wages paid to those employees that are hired on or before the expiration date of the enterprise zone.

For purposes of calculating the hiring credit, all portions of the hiring credit statute are deemed to remain in effect. Further, the enterprise zone designation is also deemed to remain in effect.

The sales or use tax credit is available for property purchased and placed in service before the expiration date of the enterprise zone. Sales or use tax paid or incurred on qualified property that is purchased and placed in service on or before October 14, 2001 can be used for purposes of computing the sales or use tax credit.

The business expense deduction is available to qualified taxpayers for qualified assets purchased and placed in service on or before the expiration date of the enterprise zone. Qualified assets purchased and placed in service on or before October 14, 2001

are eligible for computing the business expense deduction.

The enterprise zone net operating loss is allowed for the loss incurred by the taxpayer that is attributed to their activities in the enterprise zone prior to the expiration of the enterprise zone.

Any taxable year-end net operating loss that is attributed to the enterprise zone activities will be eligible for the enterprise zone net operating loss. This loss is computed by computing the enterprise zone net operating loss as if the enterprise zone had remained in existence the entire year, and then this full year loss is prorated based on the number of days the taxpayer operated in the enterprise zone for the tax year, as compared to the total number of days in the tax year.

The net interest deduction is available to taxpayers (creditors) for qualified interest payments received before the expiration date of the enterprise zone. Thus, qualified interest payments received on or before October 14, 2001 are eligible for computing the net interest deduction.

Credits and net operating loss deductions incurred before the expiration of the enterprise zone and subject to carryover will continue to be allowed after the expiration of the enterprise zone.

The limitation on the use of the credit (limited to tax on income attributed to the zone) and net operating loss deduction (limited to income attributed to the zone) will also remain in effect.

For more information, obtain FTB 3805Z Booklet, Enterprise Zone Business Booklet.

Ask the Advocate



Debbie Newcomb
Taxpayer
Advocate

Q: Will my clients' estimated tax penalty be reduced if I file an amended return reducing their tax liability?

A: It depends. The penalty will be reduced if the amended return is filed before the extended due date of the return. The penalty is based on the tax shown on the original return. The courts have held that an amended return is deemed an original return if filed before the extended due date. Conversely, if the amended return is filed after the extended due date the estimated tax penalty will not be reduced.

Research and development credit:

Pay attention to California's definition of gross receipts

California allows a credit for qualified expenses your clients incur while conducting research in California. However, California also has several exceptions to federal law that can affect your computations for the credit. When computing the amount of your clients' research and development credit, pay particular attention to how California defines gross receipts.

Revenue and Taxation Code Section 23609(h)(4), which defines the term gross receipts for the purpose of determining the California credit for research expenses, modifies the federal law relating to gross receipts (Section 41(c)(6) of the Internal Revenue Code) to take into account only those gross receipts from the sale of property held primarily for sale to customers in the ordinary course of taxpayer's trade or business that is delivered or shipped to a purchaser within this state, regardless of the freight on board point or any other condition of sale.

This particular California law affects taxable years beginning on or after January 1, 1993 and allows for two differences from federal law. 1) Gross receipts for California purposes are more limited than what's allowed under federal law, and 2) they must be from the sale of property delivered or shipped to a purchaser within this state.

This amount may be different than the amount used for the California sales factor numerator on Schedule R-1, Apportionment and Allocation of Income.

Calculating base amount

Internal Revenue Code Section 41(c)(1) defines base amount as the product of the fixed-base percentage and the taxpayer's average annual gross receipts for the four taxable years preceding the

taxable year for which the credit is being determined.

When performing this calculation you must use the California gross receipts to correctly determine the Research and Development Credit.

What to include in gross receipts

California gross receipts should include receipts from the sale of real, tangible, or intangible property held for sale to customers in the ordinary course of the taxpayer's trade or business that is delivered or shipped to a purchaser in California. This would include sales to the U.S. government, which could be identified as delivered in California.

What to exclude in gross receipts

Exclude items such as throwback sales, as well as, receipts from services, rents, operating leases, and interest.

Generally speaking you should also exclude items such as royalties and license payments. Evaluate transactions that operate as a combined sale of property and

services on a case-by-case basis, based on the terms of the contract.

When to file an amended return

You may file an amended return to correct the computation for any tax years open under the statute of limitations. In addition, carryovers from closed years may need to be revised as well. If we're conducting an ongoing audit, provide the auditor with the revised gross receipts, if they are material. In some situations, changes resulting from this interpretation might not result in any change to the credit amount if the credit is already limited to 50 percent of research and development expenditures. Changes made to gross receipts apply to the average annual gross receipts and to the base years (1984-1988). This provides consistency to the gross receipts calculation.

If you have questions or need assistance computing the research and development credit, call our Tax Practitioner Hotline at (916) 845-7057 or refer to Form FTB 1082 – Research & Development Credit: Frequently Asked Questions available on our forms and publications webpage at <http://www.ftb.ca.gov/forms/misc/1082.pdf>.

Manufacturers' Investment Credit website debuts

We now provide comprehensive information about the Manufacturers' Investment Credit (MIC) on our website.

Go to www.ftb.ca.gov/geninfo/credits/mic/references/index.html to access FTB manuals, publications, codes, regulations, notices, and rulings, and several non-Franchise

Tax Board MIC reference materials. If you need additional assistance with the MIC, call us, from within the United States, at 1.800.852.5711. From outside the United States, call 1-916-845-6500 (not toll-free).

For the hearing impaired with TDD, call 1-800-822-6268 and follow the text prompts.

Corrections to tax forms, publications, instructions

Please note the following corrections for some of our 2001 California tax forms, instructions, and booklets. If you have any questions about these or any other forms, contact our Tax Forms Development and Distribution Section at (916) 845-3442.

Corrections

Form 540-ES, *Estimated Tax for Individuals, Instructions* (contained within California 540A, *2001 California Resident Income Tax Return—Special Edition for Seniors*), pages 37 and 38 are incorrect.

The incorrect pages appear within the California Form 540A, *2001 Special Edition for Seniors* and in the first release of the CD ROM. The corrected version will appear in the second release of *Package X* on CD ROM. The Internet version is correct.

Correction

California 540NR, *2001 Nonresident or Part-Year Booklet*

On page 11, step 4 – *Taxable Income*, the first sentence appearing under *Military Pay Adjustment* should read:

If you are serving on active duty military and domicile in Arizona, Idaho, Louisiana, Nevada, Texas, New Mexico, Washington, Wisconsin, or Puerto Rico (community property states), AND your spouse is a California resident, you are entitled to an adjustment of ½ of your military pay.

This error appears in the California 540NR, 2001 Package X, and in the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form FTB 3800, *Tax Computation of Children Under Age 14 with Investment Income*

On page 1, part II, line 10, it should read:

Enter the parent's tax from Form 540, line 20; Form 540A, line 17; or Telefile Tax Record, in the box labeled "Tax." Long or Short Form 540NR filers, see instructions. Do not include any tax from FTB 3803, 2001 Parents' Election to Report Child's Interest and Dividends.

This error appears in the 2001 Package X and in the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form FTB 3805Z, *2001 Enterprise Zone Business Booklet*

On page 4, part I – *Hiring Credit*, column 3, the first paragraph should read:

Effective January 1, 2001, the established minimum wage was \$6.25 per hour. Effective January 1, 2002, the minimum wage increased to \$6.75 per hour. For purposes of computing the EZ credit, 150 percent of the minimum wage is \$9.37 per hour (\$10.12 beginning January 1, 2002).

This error appears in the 2001 Package X and the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form FTB 3805Z, *2001 Enterprise Zone Business Booklet*

On page 4, part I – *Hiring Credit*, column 3, the fourth paragraph should read:

Effective January 1, 2001, the established minimum wage was \$6.25

per hour. Effective January 1, 2002, the minimum wage increased to \$6.75 per hour. For purposes of computing the EZ hiring credit, 202 percent of the minimum is \$12.62 per hour (\$13.63 beginning January 1, 2002).

This error appears in the 2001 Package X and the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form FTB 3807, *2001 Local Agency Military Base Recovery Area Deduction Business Booklet*

On page 4, column 2, the first paragraph should read:

Where the California minimum wage is higher than the federal minimum wage, the California minimum wage is used for purposes of computing the LAMBRA hiring credit. Effective January 1, 2001, the established minimum wage was \$6.25 per hour. Effective January 1, 2002, the minimum wage is increased to \$6.75 per hour. For purposes of computing the LAMBRA hiring credit, 150 percent of the minimum wage is \$9.37 per hour (\$10.12 beginning January 1, 2002.)

This error appears in the 2001 Package X and the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form FTB 3808, *2001 Manufacturing Enhancement Area Business Booklet*

On page 3, column 3, the 5th paragraph should read:

Continued on page 6

Corrections to tax forms, publications, instructions

Continued from page 5

Where the California minimum wage is higher than the federal minimum wage, the California minimum wage is used for purposes of computing the MEA hiring credit. Effective January 1, 2001, the established minimum wage was \$6.25 per hour. Effective January 1, 2002, the minimum wage is increased to \$6.75 per hour. For purposes of computing the MEA hiring credit, 150 percent of the minimum wage is \$9.37 per hour (\$10.12 beginning January 1, 2002).

This error appears in the 2001 Package X and the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form FTB 3809, 2001 Targeted Tax Area Deduction Booklet

On page 4, column 1, the 6th paragraph should read:

Where the California minimum wage is higher than the federal minimum wage, the California minimum wage is used for purposes of computing the TTA hiring credit. Effective January 1, 2001, the established minimum wage was \$6.25 per hour. Effective January 1, 2002, the minimum wage is increased to \$6.75 per hour. For purposes of computing the TTA hiring credit for 2001, 150 percent of the minimum wage is \$9.37 per hour (\$10.12 beginning January 1, 2002).

This error appears in the 2001 Package X and the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

FTB Publication 1005, 2001 Pension and Annuity Guidelines

On page 4, column 1, entitled: *Individual Retirement Arrangements (IRAs)*, under the section entitled *1987 through 2001*, the last sentence should read:

An elective deferral of up to \$6,500 made be made to a SIMPLE IRA.

This error appears in the 2001 Package X and the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form 9000, 2001 Homeowners Assistance Claim Booklet

Page 14, *Homeowner Assistance Schedule*, should read:

If your total income is from \$11,164 to \$11,750, your percentage of assistance is 86 percent.

This error appears in the print version of the 2001 Homeowners Assistance Claim Booklet. The Internet version is correct.

Correction

Schedule D, *California Capital Gain or Loss Adjustment*, line 3 should read:

Capital gain distributions (federal Form 1099-DIV, box 2a minus box 2e)

Editor's note: Without this correction, taxpayers will be subtracting Unrecaptured Section 1250 gain (box 2d) from the total capital gain from box 2a instead of correctly subtracting the Section 1202 gain (box 2e) from the total capital gain from box 1a.

This error appears in the print version of the 2001 Personal Income Tax Booklet, 2001 Nonresident or Part-Year Booklet and the stand alone Schedule D. The Internet versions are correct.

Correction

Schedule P (541), *Alternative Minimum Tax and Credit Limitations – Fiduciaries*

The instructions on page 7, entitled: *Credit Table, Offset Tax Section* has errors relating to the B2 and B3 listings. All B2 listings should be changed to B1 and all B3 listings should be changed to B2.

These errors appear in the instructions of the stand alone, print version of the schedule. The print and CD-ROM versions of the 2001 Package X are correct. The Internet version is also correct.

Correction

Form FTB 3805Z, *Enterprise Zone Deduction and Credit Summary*

On side 2, *Worksheet VII, Computation of Credit Limitations – Enterprise Zones*, line 4 should read:

4 Enter the enterprise zone NOL deduction from Worksheet VI, Section C, line 24, column (c).

This error appears in the 2001 Enterprise Zone Business Booklet, 2001 Package X, and in the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form FTB 3807, *Local Agency Military Base Recovery Area Deduction and Credit Summary*

On side 2, *Worksheet VI, Computation of Credit Limitations – LAMBRA*, line 4 should read:

4 Enter the LAMBRA NOL deduction from Worksheet V, Section C, line 14, column (c).

Continued on page 7

Corrections to tax forms, publications, instructions

Continued from page 6

This error appears in the *2001 Local Agency Military Base Recovery Area Business Booklet*, the print version of the *2001 Package X*, and the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

Form FTB 5805F, *Underpayment of Estimated Tax by Farmers and Fishermen*

On line 9, *Part I, Figure Your Underpayment*, should read:

2000 tax after credits from Form 540, line 34; Form 540NR, line 43; or Form 541, line 25 (If you did not file a return for 2000 or if your 2000 tax year was less than 12 months, do not complete lines 9 – 11. Instead, enter the amount from line 6 on line 12.)

This error appears in *2001 Package X* and in the first release of the CD ROM. The corrected version will appear in the second release of the CD ROM. The Internet version is correct.

Correction

2001 S Corporation Tax Booklet

On page 33, line 8, *Deductions—Expense deduction for recovery property*, the first line should read:

The maximum expense deduction for recovery property you can claim from all sources is \$24,000. (IRC Section 179 deduction).

Schedule K-1 (100S) Shareholders' Instructions

On page 3 of the instructions, line 8, *Deductions—Expense deduction for recovery property*, the first line should read:

The maximum expense deduction for recovery property you can claim from all sources is \$24,000. (IRC Section 179 deduction)

These errors appear in the *2001 Package X*. The information is correct in the first release of the CD ROM. The Internet version is also correct.

Correction

Schedule K-1 (541), *Beneficiary's Share of Income, Deductions, Credits, etc.*

On line 10, *Deductions in the final year of the estate or trust*, Section A: *Excess deductions on termination*. (Attach computation), the solid line separating lines 10a and 10b should also cross columns (b), (c), (d), and (e).

This error appears in the *2001 Package X* and the first release of the CD ROM. The Internet version is correct.

Correction

FTB Publication 1067, *Guidelines for Filing a Group Form 540NR*

On Page 3, Column 1, under Section N—*Instructions for Completing Group Nonresident Return*, line 4a has been revised to read as follows:

Enter the total distributive share of California source income from Schedule 1067A, Part I, column (c), one line 25.

This error appears in the *2001 Package X* and in the first and second release of the *Package X* on CD Rom. The Internet version is correct.

Corrections to 2000 California tax forms, instructions, and booklets

Form FTB 5805F, *Underpayment of Estimated Tax by Farmers and Fishermen*

On Line 9, *Part I, Figure Your Underpayment*, line 9 should read:

l. 1999 tax after credits from Form 540, line 34; Form 540NR, line 43; or Form 541, line 25 (If you did not file a return for 1999 or if your 1999 tax year was less than 12 months, do not complete line 9 – line 11. Instead, enter the amount from line 6 on line 12.)

This error appears in the *2000 Package X* and CD Rom. The Internet version is correct.

Check out our improved FTB website

How's our website? To better serve you, we recently changed our website, www.ftb.ca.gov.

We based our changes on input from you and your clients—both informally via e-mail and phone calls, and formally through a series of focus group interviews we conducted in November. So, visit our website and let us know what you think. Send your suggestions and comments to webmaster@ftb.ca.gov.

Presorted
First-Class Mail
U.S. Postage Paid
Sacramento, CA
Permit No. 312

Tax News
PO BOX 2708
RANCHO CORDOVA CA 95741-2708
Address Service Requested